BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
RICHARD W. AND HAZEL R. HILL)

For Appellants: Richard W. Hill, in pro. per.

For Respondent: Mark McEvilly
Counsel

O P I N I O N

This appeal is made pursuant to section 19057, subdivision (a), of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claim of Richard W. and Hazel R. Hill for refund of personal income tax and penalty for failure to furnish information on notice and demand in the total amounts of $263.18 and $491.58 for the years 1973 and 1974, respectively.

The issues for determination are: whether respondent's action in disallowing the deductions claimed on appellant's 1973 and 1974 returns was correct; and whether 25 percent penalties for failure to furnish information on notice and demand were properly assessed for each year.

During the appeal years, Mr. Hill (hereinafter appellant) characterized himself as a self-employed broker-consultant. His wife was employed as an insurance company claims representative.

Prior to 1969 appellant was employed as an investment promoter and as a parking structure manager. During 1969 and the early 1970's appellant attempted to establish himself as a consultant for parking structure construction. Thereafter, appellant began soliciting advice concerning the development and marketiny of a radio program. During the appeal years appellant's activities consisted of such solicitation. However, no negotiations leading to the sale of a radio program were conducted during 1973 or 1974, although in 1978 appellant did obtain a contract to produce and air a radio show.

On the returns for the appeal years the only income reported was derived from Mrs. Hill's employment as an insurance claims representative. NO income was reported from appellant's activities. On-the 1973 and 1974 returns appellant claimed $6,367.87 and $7,860.19, respectively, in expenses incurred in connection with his activities.

On four occasions during 1976 respondent attempted unsuccessfully to arrange for an audit of appellant's 1973 and 1974 returns. Finally, on December 29, 1976 respondent made formal demand upon appellant for information regarding the claimed expenses. Appellant made no effort to comply. On March 29, 1977 respondent issued the notices of proposed assessment in question. On June 17, 1977, having received no response from appellant, the proposed assessments were affirmed. Thereafter, respondent collected the total amounts due for 1973 and 1974 by attaching funds from appellant's savings account. In May of 1978 appellant filed a claim for refund.

In September of 1979 appellant met with respondent to consider the claim for refund. At the meeting appellant was able to substantiate some of the expenses claimed for 1973 but was unable to substantiate any of the expenses claimed for 1974. Respondent determined that the claimed expenses were not deductible because they were

incurred to establish a new trade or business and not incurred in "carrying on any trade or business." Furthermore, respondent determined that the evidence offered to substantiate the claimed expenses, which was for 1973 only, was inadequate. This appeal followed.

Section 17202 of the Revenue and Taxation Code provides for the deduction of all "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." However, it is well settled that expenses incurred in investigating and looking for a new business, as opposed to expenses incurred in carrying on an existing business, are not deductible. (See Richmond Television Corporation v. United States, 345 F.2d 901 (4th Cir. 1965); William Tiffin Downs, 49 T.C. 533 (1968); Morton Frank, 20 T.C. 511 (1953); Jack Pershing Stanton, ¶67,137 P-H Memo. T.C. (1967); Appeal of Howard and Margaret Richardson, Cal. St. Bd. of Equal., Feb., 1976.)

Ordinary and necessary expenses are deductible only when related to the carrying on of a trade or business. The concept of a trade or business does not encompass all activities engaged in for profit, but is used in the realistic and practical sense of a going trade or business. (William Tiffin Downs, supra.) Even though a taxpayer has decided to enter into business and, over a considerable period of time, spent money in preparation for entering that business, he still has not engaged in carrying on a trade or business within section 17202 until such time as the business has begun to function as a going concern and performed the activities for which it was intended. (Richmond Television Corporation v. United States, supra.)

In order to prevail on this issue appellant has the burden of connecting the expenditures in issue to an existing trade or business. (Jack Pershing Stanton, supra.) According to the meager record in this appeal, prior to the appeal years appellant had been engaged as a consultant for parking structure construction. During the appeal years appellant was gathering information concerning the development and marketing of radio programs, a new and different endeavor. Appellant has offered nothing to connect any expenditure incurred during the appeal years with the radio show which was developed in 1978, well after the years in issue. Therefore, we must conclude that any expenses incurred during 1973 and 1974 were not incurred in carrying on an existing trade or business and are not

deductible. In view of this determination it is not necessary to consider whether the substantiation offered by appellant in support of the 1973 expenses was adequate.

Section 18683 of the Revenue and Taxation Code provides that respondent may assess a 25 percent penalty if a taxpayer fails or refuses to furnish any information requested in writing by respondent unless such failure is due to reasonable cause and not willful neglect. Appellant has not specifically contested the imposition of this penalty and we can find nothing in the record which would suggest that appellant's failure to provide the requested information was due to reasonable cause. Accordingly, we must conclude that respondent properly imposed the penalty.

For the reasons discussed above, respondent's action in this matter must be sustained.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claim of Richard W. and Hazel R. Hill for refund of personal income tax and penalty for failure to furnish information on notice and demand in the total amounts of $263.18 and $491.58 for the years 1973 and 1974, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 19th day of May , 1981, by the State Board of Equalization, with all Board members present.

Ernest J. Dronenburg, Jr. , Chairman

George R. Reilly , Member

William M. Bennett , Member

Richard Nevins , Member

Kenneth Cory , Member